Quarterly Economic Indicator

Scottish Chambers of Commerce Network

RESULTS: QUARTER 3 2022

in partnership with
Fraser of Allander Institute

CONTENTS

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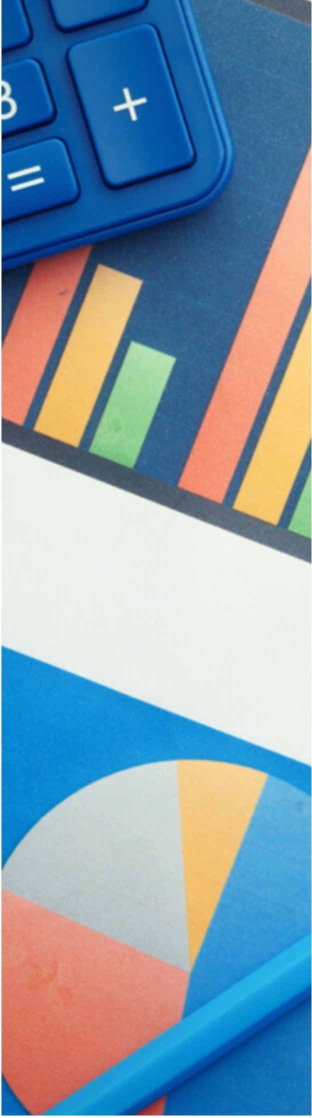


Foreword

Mairi Spowage
Director
Fraser of Allander Institute

It has felt like the most extraordinary few weeks of political turmoil. The "mini" budget and the associated market turbulence has put upward pressure on the costs of government borrowing – and in turn, the costs of borrowing across the economy.

The U-turns we have seen have, at the time of writing, calmed the markets somewhat. The new chancellor will be setting out his Medium-Term Fiscal Plan on 31st October. Given the mistakes that have been made by his predecessor, it is likely that Jeremy Hunt will have to go further in terms of spending restraint and potential tax rises compared to what may have been the case without the chaos.

The review of the energy price guarantee after April will obviously cause concern for households given the projected rise in prices which had been expected in April. It will be crucial to see how the Government choose to support households after April – and also the impact this could have on measured inflation depending on the way the Government chooses to intervene.

Following the Chancellor's statement, there will be the next Bank of England Rate decision on 3rd November. This is widely expected to be another significant rate rise.

New inflation data was published this week which showed that the headline rate is again into double digits at 10.1%. Of course, this is the experience for consumers – the data also shows that input inflation for businesses continues to run well above that experienced by consumers. This is borne out by the survey results, which shows a record high level of concern amongst businesses about this.

Closer to home, we are expecting the Scottish Government to present their Emergency Budget review next week.

Whilst this is likely to focus on areas where further savings have been identified to help fund public sector pay settlements, it will be interesting to see what further measures are announced to support households and businesses through the next few months. Taxation announcements are likely to be kept for the Scottish Budget, now on the 15th December.

Introduction

Stephen Leckie
President
Scottish Chambers of Commerce

Frozen investment, faltering confidence, falling cashflow and profits, and a pessimistic global outlook, paint a concerning picture for businesses in Scotland.

There is more pressure to come in the winter months. The signs of an economic bounce back don't look promising as more and more firms are telling us that they have been forced to cancel contracts, projects or plans to expand, due to soaring costs and difficulty in hiring people.

Whilst we recognise the strain that has been placed on the public finances, governments in Edinburgh and London must make clear how businesses will be supported to survive through the difficult months ahead and what measures will be put in place to support long-term growth.

The Scottish Government's Emergency Budget – which also faces immense budgetary pressures – must set out how it intends to protect businesses and industries from the worst effects of the mounting costs crisis. It should also set out how Scotland's taxation policies such as income tax and LBTT will apply competitiveness to help attract investment and create jobs.

The emergency budget as well as the December Budget should do more to ease the overall cost burdens on business. The main cost burden on firms could be reduced by cutting the headline poundage rate of Non-Domestic Rates, and delaying changes to the NDR appeals system which are set to add significant bureaucracy and costs to firms.

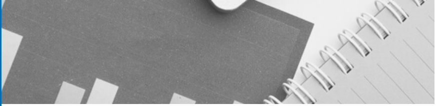
Energy bills continue to be the most pressing cost pressure for firms. The decision by the UK Government to roll back on the energy support for households and firms from next April is a major concern. We urge the Chancellor to engage with the business community urgently and provide clarity on the proposed targeted support beyond April for the most vulnerable sectors and avoid cliff edge scenarios.

With the Bank of England set to raise interest rates again in the coming weeks, businesses are caught between rising input and borrowing costs. We need to see a clear long-term economic prospectus from the UK Government which will provide a stable environment for investment.

QUARTERLY ECONOMIC INDICATOR

Key Findings

Quarter 3 2022



The Q3 2022 survey was conducted between August & September 2022. 280 firms responded to the survey.

Inflation Rermains Top Concern:

- Last quarter saw record high level of concern from inflation, cited by 92% of all firms. While it has eased over the quarter, it remains at significantly high levels for the survey at 88% of all firms, compared to the average of 35% from 2018 – 2021.

Cashflow & Profits Falling:

- Cashflow and profits remain weak across all sectors, highlighting the growing impact of cost pressures. Compared to the previous quarter, the construction and manufacturing sectors saw the most significant falls in confidence.

Energy Bills Top List of Cost Pressures:

- The top cost pressure is from utilities such as electricity and gas with it being cited by 80% of firms, followed by labour costs at 72% and then fuel costs at 63% of firms.

·Firms Still Planning to Raise Prices:

- 8 in 10 of all firms indicate that they intend to raise the prices that they charge over the next quarter. This is a record high for the survey and a figure which has grown exponentially over the year. In comparison, 50% of all firms said they would increase their prices in Q3 2021 last year.

Labour Market Pressures:

- Recruitment difficulties have seen a 10% increase from the previous quarter, with half of all firms reporting increased challenges hiring staff. The sectors that saw the largest increases from Q1 2022 were the financial and business services, manufacturing and retail sectors.

Struggling Confidence:

- On balance, all firms have reported a fall in confidence compared to the previous quarter and a more significant fall compared to last year. On a sectoral basis, construction, retail and tourism sectors all reported falls on balance.

CONSTRUCTION

Inflation:
Concern from inflation continues to dominate the construction sector, with 9 in 10 firms still seeing it as a threat.

Cost Pressures:
The leading cost pressures remain utility costs, labour costs and raw material prices, with at least 6 in 10 firms being significantly affected by these.

Cashflow & Profits:
Firms have reported falls on balance in levels of cashflow and profits, for the third quarter in a row.

Contracts & Sales:
While sales trends have remained positive, this is in contrast to contract trends which have all reported negative net balances for the first time since Q3 2020.

Investment:
Most firms for each investment trend have reported no changes to their investment levels. On balance, firms expect investment to fall in Q4 2022.

BUSINESS VOICE:

“Really not sure what is going to happen with the increase in costs. Business are having to put their prices up and clients/customers are reducing spend as they too are struggling. Government need to step in urgently."
Construction firm in Moray

FINANCIAL & BUSINESS SERVICES

Inflation:
A successive record high of 82% of firms have reported increased concern from inflation. This is almost double the level of concern recorded for Q3 2021.

Cost Pressures:
The leading cost pressures for firms remain utility costs (65%) and labour costs (54%). Most cost pressures saw an increase over the quarter.

Sales & Orders:
Most sales trends have remained at positive net balances, except for online sales which saw a fall on balance. The net balance of +13% for total sales is the lowest growth reported for this trend in over a year.

Labour Market:
As has been a familiar trend throughout 2022, at least half of firms are reporting no changes to staff levels. 60% of firms reporting recruitment difficulties is a successive record high.

Price Rises:
A new record 63% of firms reported that they intend to increase their prices in the next quarter, eight percentage points above the previous record set last quarter.

BUSINESS VOICE:

“My big concern is what's coming up as the true cumulative economic impact of energy costs on businesses won't be fully felt until more supply contracts expire. What a lottery that the chances of survival of a small business should be so dependent upon your contract date." - Services firm in Dundee

MANUFACTURING

Inflation:
Inflation remains the top concern for firms in the sector with 84% of firms reporting concern from it over the quarter. This has been consistently high over the past year.

Cost Pressures:
For a second successive quarter, at least 8 in 10 firms have reported raw material prices and utility costs as the top cost pressures.

Labour Market:
Recruitment difficulties have increased by 5 percentage points to 61% of firms. This is around 18 percentage points higher than the Q3 average.

Cashflow & Profits:
Firms have reported negative net balances for both cashflow and profits, after what had been signs of resilience earlier in 2022. Both trends sit well below the five-year survey average.

Confidence:
Firms in the sector have reported a positive net balance for the eighth successive quarter, albeit significantly eased since last quarter.

BUSINESS VOICE:

"Rising costs are a real worry and redundancies are the result. The Deposit Return Scheme coming live in August 2023 is a massive concern as the costs and admin involved are unworkable for small producers."

- Manufacturing firm in the Lothians

RETAIL & WHOLESALE

Inflation:
A record near 9 in 10 (88%) report concern from inflation, a five-percentage point rise from the previous record high last quarter.

Cost Pressures:
The leading cost pressures remain utility costs (80%), raw material prices (65%) and labour costs (63%).

Labour Market:
Firms have reported a fall on balance in employment for the first time since Q2 2021. The percentage of firms actively recruiting staff (45%) has fallen to its lowest in over two years.

Confidence:
Retail firms have reported, on balance, a fall in confidence for the second successive quarter. Confidence is down 33 percentage points since Q3 2021.

Cashflow & Profits:
Firms have reported negative net balances for cashflow and profits, for a fourth succesive quarter. Although eased compared to the previous quarter, it is still a significant drop-off since last year.

BUSINESS VOICE:

"Very concerned about the reduced levels of spend from customers when they have less disposable income. Balancing increased prices of raw materials against not increasing our own prices to lose sales is challenging."

- Retail firm in the Scottish Borders

TOURISM

Inflation:
Concern from inflation saw a rise of 11 percentage points, to a new record high 94% of firms. This is 34 percentage points higher than Q3 2021.

Cost Pressures:
The leading cost pressures remain utility costs (91%), labour costs (86%) and fuel costs (66%). All these trends have seen sizeable increases over the quarter.

Price Rises:
Over 7 in 10 firms (72%) expect to raise their prices in Q4 2022. While eased since the record high of the previous quarter, this remains significantly high for the sector.

Cashflow & Profits:
Strong sales have contributed to a positive net balance (+12%) for cashflow, for the first time in a year of the survey. Profits have reported a negative net balance (-4%) for the fourth successive quarter.

Confidence:
Confidence among tourism firms has been fragile in 2022 and that continues this quarter, with nearly half of firms (49%) reporting a fall in confidence.

BUSINESS VOICE:

"Hospitality VAT is too high - we are constantly trying to save for the VAT return but it's a real struggle. There is never any money left for investment or profit. We don't know if we have enough cashflow and business to get through the winter. We haven't had a good summer to get us through the winter." - Tourism firm in the Highlands

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